 CONGRESSIONAL AFFAIRS

86-0751

SPECIAL

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

March 11, 1986

LEGISLATIVE REFERRAL MEMORANDUM

TO: Legislative Liaison Officer -

Department of Defense
Department of State
Central Intelligence Agency
United States Postal Service
District of Columbia

SUBJECT: Office of Personnel Management Advance draft bill, "To amend title 5, United States Code, to reform the Civil Service Retirement System, and for other purposes."

This proposal would implement the President's Fiscal Year 1987 Budget recommendations and requires expedited handling.

The Office of Management and Budget requests the views of your agency on the above subject before advising on its relationship to the program of the President, in accordance with OMB Circular A-19.

A response to this request for your views is needed no later than WEDNESDAY, MARCH 19, 1986.

Questions should be referred to Hilda Schreiber (395-7362) the legislative analyst in this office.

Naomi R Sweeney

Naomi R. Sweeney for
Assistant Director for
Legislative Reference

Enclosures

SPECIAL

UNITED STATES
OFFICE OF PERSONNEL MANAGEMENT
WASHINGTON, D.C. 20415

Office of the Director

Rec'd LRD
12 noon
3-11-86

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Honorable George Bush
President of the Senate
Washington, D.C. 20510

Dear Mr. President:

The Office of Personnel Management submits herewith a legislative proposal, "To amend title 5, United States Code, to reform the Civil Service Retirement System, and for other purposes." This proposal would implement recommendations contained in the President's budget for fiscal year 1987. We request that you refer this proposal to the appropriate committee for early consideration.

At present, the Civil Service Retirement System is extremely expensive, having a dynamic normal cost of nearly 35 percent of payroll, which is considerably more than private sector pension plans cost. Furthermore, the System has a massive unfunded liability of $542.1 billion as of September 30, 1984--more than a half trillion dollars of debt. Even ignoring the unfunded liability resulting from future pay raises and future cost-of-living adjustments, the unfunded liability (the so-called "static" unfunded liability) was $190.6 billion in 1984.

In order to deal with the excessive cost of the Civil Service Retirement System, and its huge debt, and in order to bring its benefits more into line with private sector pension plans, this draft bill would make several changes in the System, while preserving an adequate level of retirement income for Federal employees.

Under the proposal, the determination of an individual's average pay for the purpose of computing retirement benefits would use the highest earnings over a five-year period, rather than three years as at present. This change would not take effect until October 1, 1989, and would not affect anyone eligible to retire by that date.

Beginning in 1987, employee and agency contributions to the System would be increased from 7 percent each to 9 percent each. In addition, the proposal would require the United States Postal Service and the District of Columbia government to contribute to the Civil Service Retirement and Disability Fund an additional 2 percent of basic pay each year until their payments, when combined with employee deductions, are sufficient to cover the dynamic normal cost of the Retirement System.

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Although no change would be made in the age at which individuals may retire, a reduction in benefits for retirement before age 62 would be phased into the program. Currently, unreduced benefits are available to individuals with thirty years of service who retire as early as age 55. Under the proposal, benefits would be reduced by 2 percent a year for each year the individual is under age 62 at the time of retirement. This change would not affect anyone who reaches age 55 by October 1, 1986.

Several changes would be made with respect to cost-of-living adjustments (COLA's) in Civil Service Retirement annuities. First, the adjustment scheduled for December 1986 would not take effect. Then, beginning with the December 1987 COLA, adjustments would be based on the percentage change in the Consumer Price Index (CPI) less 2 percentage points. With the exception of the elimination of the December 1986 COLA, these COLA changes are not intended to affect military retirees, and a provision in the bill would exclude military retired and retainer pay from application of the changes in the COLA methodology in future years.

The proposal would also change the method of computing benefits for employees who perform part-time service, so that benefits would be proportional to the service actually performed. The change would apply only to service performed on or after October 1, 1986, and would not affect annuity eligibility.

Eligibility rules for surviving spouses, former spouses, and individuals named as having an insurable interest in the employee or Member would be changed to parallel more closely the treatment of similarly situated survivor beneficiaries under the Social Security System. Benefits would not be payable for any month during any portion of which the widow, widower, former spouse, or insurable interest designee has not reached age 60, has not attained age 50 if disabled, or does not have in his or her care a surviving child of the employee, Member, or annuitant.

A further change would be the phasing out of survivor benefits for post-secondary students. This change would be consistent with one made in the Social Security System several years ago. Also in an effort to be consistent with Social Security, the proposal would revise commencing dates and termination dates of annuities so that benefits would be payable only for full months.

It should be noted that, except for the reduction in annuities for early retirement, the changes proposed here can be effected administratively for the Foreign Service and Central Intelligence Agency retirement systems.

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Employees of the government of the District of Columbia hired on or after October 1, 1986, would be excluded from the Civil Service Retirement System, the Federal Employees' Group Life Insurance Program, and the Federal Employees Health Benefits Program. In view of the District's authority under home rule to manage its affairs with less dependence on the Federal Government, it is no longer appropriate for District employees to be carried under the benefit programs for Federal employees.

We estimate that the proposed changes in Civil Service Retirement would reduce the budget deficit (i.e., increase receipts or reduce outlays) by the following amounts:

Fiscal Year 1987	$ 1,604 million
Fiscal Year 1988	2,571 million
Fiscal Year 1989	3,179 million
Fiscal Year 1990	3,842 million
Fiscal Year 1991	4,411 million
1987-91 total	$15,607 million

This proposal implements a key fiscal year 1987 Budget recommendation designed to reform the high costs and generous benefits of the current System.

The Office of Management and Budget advises that enactment of this proposal would be in accord with the program of the President.

A similar letter is being sent to the Speaker of the House of Representatives.

Sincerely,

Constance Horner
Director

Enclosures

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STATEMENT OF PURPOSE AND JUSTIFICATION

To accompany a draft bill

"To amend title 5, United States Code, to reform the Civil Service Retirement System, and for other purposes."

At present, the Civil Service Retirement System is extremely expensive, having a dynamic normal cost of nearly 35 percent of payroll, which is considerably more than private sector pension plans cost. Furthermore, the System has a massive unfunded liability of $542.1 billion as of September 30, 1984--more than a half trillion dollars in debt. Even ignoring the unfunded liability resulting from future pay raises and future cost-of-living adjustments, the unfunded liability (the so-called "static" unfunded liability) was $190.6 billion in 1984.

In order to deal with the excessive cost of the Civil Service Retirement System, and its huge debt, and in order to bring its benefits more into line with private sector pension plans, the draft bill would make several changes in the System, while preserving an adequate level of retirement income for Federal employees.

"High-Five-Year" Average Salary

Since 1969, Civil Service annuities have been computed based on each employee's highest average annual earnings during 3 consecutive years. Before 1969, a " high-five-year" rather than a "high-three-year" average salary was used. This bill would return to the "high-five-year" salary. This change would not apply to anyone who is eligible to retire on or before October 1, 1989, when the provision would become effective.

Increase in Retirement Contributions

The last increase in retirement contribution rates took effect in 1970. In view of the level of benefits provided by the System, this bill would require the long overdue and entirely warranted increase in agency and employee contributions of two percentage points each beginning in January 1987.

Reduction in Annuities Payable Before Age 62

Currently, employees may retire involuntarily at age 55 after 30 years of service, at age 60 after 20 years of service, or at age 62 after 5 years of service. This bill would not change the ages at which employees become eligible to retire, but it would phase in over 4 years a reduction in

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benefits for individuals who retire before age 62. For those who are age 54 on October 1, 1986, the reduction would be 0.5 percent for each year they are under age 62 at the time of retirement. This factor would rise gradually with respect to younger individuals until it reached 2 percent for individuals who are 51 years old or younger on October 1, 1986. Those who are 55 or older on October 1, 1986, would have no reduction in their annuities. The reduction would not apply to law enforcement officers, firefighters, or other special groups. The reduction would encourage individuals to work beyond the date of their earliest retirement eligibility and would require those who do retire early to bear a more reasonable portion of the high cost of early retirements.

Limit on Cost-of-Living Adjusments

Under 5 U.S.C. 8340, an annual cost-of-living adjustment (COLA) is ordinarily effective on December 1 of each year (and is first paid in the annuity checks issued at the beginning of January), based on the rise in the Consumer Price Index (CPI) between the third quarter of that calendar year and the third quarter of the preceding calendar year. Under this proposal, the adjustment scheduled for December 1986 would not take effect. Then, beginning with the December 1987 adjustment, the COLA amount each year would be the CPI change minus two percentage points.

These proposed changes are designed to bring Federal annuitants into closer alignment with other retired people who typically receive full regular COLA's on only their Social Security benefits, and to remove the disincentive for retirement-eligible Federal employees to continue working as retirement benefits rise at a faster rate than pay.

These COLA changes would also apply to certain other retirement systems for Government employees, such as the Foreign Service Retirement System, under which COLA's are linked to Civil Service Retirement COLA's. Except for the elimination of the December 1986 COLA, these changes would not apply to military retired and retainer pay COLA's.

Computation of Annuities for Part-Time Employment

Currently, most employees covered by the Civil Service Retirement System receive full service credit for their part-time service, while having their salaries prorated in the computation of their annuities. Those who work part-time for a whole career receive an appropriately smaller annuity. However, if at the end of a long part-time career an employee changes to a full-time schedule for his last three years, the increase in the average salary produces an annuity equal to that received by an employee who has worked full-time for an entire career. This bill would eliminate that possibility of abuse by amending the law to provide that, for part-time service performed after September 30, 1986, the annuity would be computed under the appropriate formula multiplied by a fraction which expresses the ratio between the actual service and a full-time tour of duty for the employee's career. Thus, an employee with ten years of service performed on a half-time basis after that date and ten years of full-time service would have his benefit as computed under the appropriate formula multiplied by three-fourths to determine his annuity. In addition, to the extent that part-time service is involved, the average pay will be determined on the basis of the full annualized rate of pay for the individual's position. Computations involving disability retirement or the limitation on initial annuity payments of 80 percent of average pay would continue to use prorated salary rates that bear the same relationship to the full annual salary of the employee's position as the employee's part-time schedule bears to a full-time schedule. There would be no effect on the benefits of full-time employees, or employees who work a consistent part-time tour. Employees of the Department of Medicine and Surgery of the Veterans Administration are already subject to revised computation provisions. In order to maintain consistency, service performed by individuals from that organization after September 30, 1986, will be subject to the Government-wide provision. The Office of Personnel Management will be authorized to develop an appropriate method for computing benefits if an individual has performed part-time service before and after the date of the change in treatment of part-time service.

Survivor Benefits for Widows, Widowers, and Insurable Interest Designees

Benefits are currently payable to widows or widowers of deceased employees, Members, or annuitants, or the persons named as having an insurable interest in deceased annuitants, generally without regard to age, health, or family status. This differs markedly from the private sector where individuals are covered by Social Security under which such factors are significant in determining eligibility for survivor benefits. Accordingly, this proposal would bring the Retirement System more nearly into line with Social Security by providing that survivor benefits would not be payable for any month during any portion of which the widow, widower, or insurable interest designee has not attained age 60, has not reached age 50 if disabled, or does not have in his or her care a surviving child of the employee, Member, or annuitant.

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Survivor Benefits for Adult Students

Survivor benefits which are now payable to young adults between ages 18 and 22 who are full-time students in post-secondary schools would be eliminated by the proposal. These changes are designed to eliminate from the retirement program the responsibility for providing post-secondary educational assistance, and are prompted by similar changes made to the Social Security program by the Omnibus Budget Reconciliation Act of 1981. Future recipients would be allowed to continue benefits beyond age 18 only until the earlier of completion of secondary school or attainment of age 19. Current recipients would be permitted to continue under the program until they reach age 22 or leave school, whichever comes first.

Commencing and Termination Dates of Annuities

The proposal incorporates technical changes in the provisions governing commencement and termination of annuities so that benefits would be payable for full months only. Thus, the complex processing of lump-sum payments for partial months would be eliminated and the Retirement System would be made more consistent with the Social Security System.

Exclusion of D.C. Government Employees

Currently, employees of the government of the District of Columbia are covered by the Civil Service Retirement System, the Federal Employees' Group Life Insurance Program, and the Federal Employees Health Benefits Program. Consistent with the concept of home rule for the District of Columbia, individuals hired by the government of the District of Columbia after September 30, 1986, would be excluded from the Federal retirement, life insurance, and health benefits programs.

Contribution Rates for Postal Service and D.C. Government

The rates at which agencies contribute to the Retirement Fund currently parallel the rates paid by employees. This is true even for purportedly financially self-sufficient entities such as the Postal Service and the D.C. government. Under this proposal, these two entities would be charged the difference between the dynamic normal cost of the Retirement System (as determined by the Board of Actuaries) and the employee contribution rate, thus ending a substantial, hidden Federal subsidy to these entities. This change would be phased in by adding 2 percent each year to the agency contribution rate until the correct contribution rate is reached.

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A BILL

To amend title 5, United States Code, to reform the Civil Service Retirement System, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Civil Service Retirement Reform Act of 1986".

Sec. 2. Chapter 83 of title 5, United States Code, is amended--

(1) in section 8331--

(A) by repealing paragraph (1)(G);

(B) by repealing paragraph (1)(iv);

(C) in paragraph (4) by striking out "3" both times it appears and inserting in lieu thereof "5";

(D) in paragraph (7) by striking out ", the government of the District of Columbia,"; and

(E) in paragraph (20)--

(i) in subparagraph (B) by inserting "and" after the semi-colon at the end thereof;

(ii) in subparagraph (C) by striking out "and" after the semicolon at the end thereof; and

(iii) by repealing subparagraph (D);

(2) by repealing section 8332(b)(9);

(3) in section 8334--

(A) in subsection (a)(1) by amending the first sentence to read as follows: "The employing agency shall deduct and withhold from the basic pay of an employee, a Congressional